



Department of Energy

Bonneville Power Administration
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EXECUTIVE OFFICE

June 15, 2006

In reply refer to: LP-7

To Customers, Constituents, Tribes and Other Stakeholders:

The Bonneville Power Administration (BPA) and Southern California Edison (SCE) have reached a potential settlement agreement on two of three lawsuits filed against BPA by SCE in the Court of Federal Claims. These claims resulted from a series of complex disputes related to a 20-year power sales and exchange agreement between BPA and SCE, which BPA ultimately terminated in 2001.

BPA believes this settlement is in the best interest of BPA ratepayers because it resolves long-standing and potentially expensive litigation at a modest cost. This cost may be offset by payments BPA believes it is owed by a variety of California parties in the ongoing California Refund process. The proposed settlement agreement also helps put the fallout of the West Coast energy crisis behind BPA while protecting Northwest ratepayers and reestablishing a collaborative business relationship with an important business partner in California.

Under this proposed settlement agreement, BPA would pay SCE a settlement amount of \$28.5 million. While one of the three claims remains unresolved, settlement of two of the claims accounts for approximately \$208 million of the roughly \$240 million in damages claimed by SCE.

Background

The three outstanding claims involve a 20-year power sale and exchange agreement executed by BPA and SCE in 1988. In 1999, BPA exercised its right to terminate the contract on five years notice, which meant that in 2004, BPA would owe SCE a termination fee of \$15 million. A dispute arose later in 1999, when the parties encountered problems with the implementation and interpretation of a provision of the contract that allowed SCE to purchase option capacity from BPA. Later in 2000, SCE raised objections when BPA converted the agreement from an energy-sale to an energy-exchange. Finally, in late 2000 and continuing through 2001, issues arose with SCE's obligation to make return deliveries of the exchange energy. Ultimately, the parties could not resolve the various contract issues, and BPA terminated the agreement for default in 2001. BPA took the position that this termination superseded the earlier termination, so that it owed SCE no termination fee.

Subsequent to the termination for default, SCE filed three separate claims for damages against BPA. The first claim alleged BPA improperly converted the agreement to an energy-exchange for the 2000-2001 period. SCE alleges damages in excess of \$185 million for this claim. The

second claim alleges that BPA wrongfully terminated the agreement for default in 2001. SCE asserted that this early termination entitled them to \$22 million under the contract termination fee schedule in the contract. The third claim alleged that BPA improperly changed the price for the option capacity in the contract, and requests approximately \$32 million in damages. In total, SCE sought damages of almost \$240 million for these claims.

Proposed Settlement

Under the proposed settlement agreement, BPA would pay SCE \$28.5 million, with interest, in return for the settlement of SCE's first and second claims. SCE's third claim, which seeks approximately \$32 million in damages, remains in litigation. While the settlement would encompass only two of the three claims filed by SCE, those two claims constitute roughly \$208 million of \$240 million total damages claimed by SCE. The settlement thereby mitigates almost 87 percent of the potential financial exposure to BPA associated with continued litigation.

Additionally, the settlement contains a number of unique features that are designed to moderate the financial impacts of the payout to SCE. One such feature is the timing of the payment of the \$28.5 million to SCE. SCE agreed to be flexible in terms of the timing of BPA's settlement payment. The settlement agreement provides that BPA's obligation to pay SCE the settlement amount is not due until BPA's own claims in the California refund proceeding have reached a final resolution. The California refund proceeding, now pending before the Federal Energy Regulatory Commission and the subject of many claims and lawsuits, seeks to resolve complaints of numerous parties engaged in the power market when prices rose to unprecedented levels in 2000-2001. BPA believes it should receive a substantial sum for power it delivered to California, but was never paid for. The SCE settlement is structured so that the SCE settlement payment will be paid only when the California refund proceedings are resolved and the net amount, if any, due to BPA has been received in its entirety.

Another feature of the settlement ties the interest rates between the settlement and the claims by and against BPA in the California refund proceeding together. Under the settlement, BPA pays interest on the \$28.5 million until the California refund proceeding is complete and SCE is paid. BPA will pay interest on the settlement amount at the same effective interest rate as apply to payments to and by BPA in the California refund process. Thus, whatever the effective interest rate BPA receives or pays in the California Refund process, SCE will receive the same effective interest rate on the \$28.5 million settlement payment.

How to comment

BPA is seeking your comments on this proposed settlement. The comment period is open through July 14, 2006. Comments can be submitted on-line at: <http://www.bpa.gov/comment>, via e-mail to comment@bpa.gov, via mail to: Bonneville Power Administration, Public Affairs Office - DKC-7, P.O. Box 14428, Portland, OR, 97293-4428, or faxed to 503-230-3285. You can also call us with your comments, toll free at (800) 622-4519. Please reference the SCE proposed settlement agreement with your comments.

A copy of the proposed settlement is available online at
http://www.bpa.gov/Corporate/public_Affairs/Comment_Listings/SCE_Settlement/settlement_agreement.pdf.

Following the close of comment BPA must respond to SCE with its intention to proceed with the settlement within 30 days. In the meantime, SCE will be working with the California Public Utilities Commission seeking approval on this settlement as well.

If you have any questions, please contact your Power account executive, constituent account executive or tribal account executive. You can also call us toll free at (800) 622-4519.

Sincerely,

/s/ Stephen J. Wright

Stephen J. Wright
Administrator and Chief Executive Officer